DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

OFFICE OF
CHIEF COUNSEL

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UIL: 2056-00.00
The Honorable Carl Levin
United States Senate
Washington, D.C. 20510-2202

Attention: Daniel Levin

Dear Senator:

I am responding to your letter dated March 10, 2000, to Mr. Floyd Williams, National Director for Legislative Affairs, Internal Revenue Service, regarding the denial of the estate tax marital deduction to estates with non-citizen surviving spouses. You requested comments on the accuracy of the interpretation of Section 5033 of the Technical and Miscellaneous Revenue Act of 1998 (the TAMRA provision) contained in your letter.

Your letter generally reflects an accurate representation of the effects of the TAMRA provision. In general, the TAMRA provision disallows the unlimited marital deduction where the surviving spouse is not a U.S. citizen, unless the surviving spouse becomes a U.S. citizen by a certain date or the assets passing to the non-citizen surviving spouse are placed in a "qualified domestic trust" (QDOT).

The TAMRA provision ensures eventual inclusion of the estate in U.S. tax base

You are correct that the TAMRA provision applies equally to all non-citizen spouses, rather than only to those who give up U.S. residence and thereby avoid U.S. transfer taxes. The marital deduction defers the estate tax on the assumption the assets in the estate, if not consumed, will ultimately be included in the surviving spouse's U.S. estate. The legislative history indicates the Congress believed the surviving spouse's U.S. estate would more likely be taxed if the surviving spouse is a U.S. citizen rather than a non-citizen. While a U.S. citizen surviving spouse would have to give up both citizenship and residence to avoid U.S. estate and gift taxes (transfer taxes), a non-citizen surviving spouse would have to give up merely residence to avoid U.S. transfer taxes. The TAMRA provision is intended to ensure eventual inclusion of the estate in the U.S. tax base.

Only income and hardship distributions escape transfer taxes

You are also correct that if the assets passing to the surviving spouse are placed in a QDOT, the only amounts that may be distributed to the surviving spouse free from U.S. transfer taxes are income of the QDOT and amounts distributed due to hardship. All other distributions to a non-citizen surviving spouse from a QDOT are subject to U.S. transfer taxes.

Statistics are unavailable

You requested statistics regarding the number of people affected by the TAMRA. Unfortunately, we have been unable to obtain that information. The Statistics of Income (SOI) Division of the Internal Revenue Service collects and processes statistical data based on information reported on federal tax returns filed by U.S. taxpayers. The SOI Statistical Information Services office told us they do not collect the data you requested.
I have enclosed a brief summary explaining in more detail the operation of the QDOT provisions. I hope this information will be of assistance to you. If you have any questions, please contact   of this office at (202) 622-3850.

Sincerely,

Benedetta Kissel
Deputy Associate Chief Counsel (International)

Enclosure

Qualified Domestic Trusts

Background

Prior to the enactment of the Technical and Miscellaneous Revenue Act of 1988 (the "Act"), section 2056 of the Internal Revenue Code provided an unlimited estate tax marital deduction for estates of United States citizens or residents regardless of the citizenship of the surviving spouse. The Act, which added section 2056A to the Code, placed restrictions on the availability of the estate tax marital deduction, for estates of people dying after November 10, 1988, if the surviving spouse is not a United States citizen.

Requirements

For people dying after November 10, 1988, if the surviving spouse is not a United States citizen, no marital deduction is allowed to the decedent spouse's estate unless such property passes to the surviving spouse in a "qualified domestic trust" ("QDOT"). A QDOT is a trust that otherwise satisfies the requirements for a marital deduction under specified provisions of the Code. Section 2056A also provides that: (1) the trust instrument must require that at least one trustee of the trust be an individual citizen of the United States or a domestic corporation; (2) the trust must provide that no distribution, other than a distribution of income, may be made from the trust unless a trustee who is an individual citizen of the United States or a domestic corporation has the right to withhold from the distribution the tax imposed by section 2056A(b) on the distribution; (3) the trust must meet any additional requirements as prescribed by regulations to ensure collection of any tax imposed; and (4) the executor must make an irrevocable election on the decedent's estate tax return to treat the trust as a QDOT. Even though the requirements for qualifying as a QDOT have been modified several times since the 1988 Act, the requirements as provided above are applicable for all people dying after November 10, 1988.

Taxation

Under section 2056A(b), a deferred estate tax is imposed when certain "taxable events" occur. In general, distributions of principal from the QDOT during the surviving spouse's lifetime constitute taxable events. The tax is also imposed on the value of the trust (1) at the time of the noncitizen surviving spouse's death or (2) if the trust ceases to meet the requirements of a QDOT. Distributions of income from a QDOT to a noncitizen surviving spouse and distributions of principal to the surviving spouse on account of "hardship" are exempted from the QDOT tax.

If a taxable event occurs during the surviving spouse's lifetime, the amount on which the QDOT tax is imposed is the amount of cash and the fair market value of the property that is subject to the distribution, including any amount withheld from the distribution by the U.S. trustee to pay the tax or any tax paid by the QDOT for the distribution. The amount taxed at the death of the surviving spouse is the fair market value of the trust assets at the date of the surviving spouse's death. If a taxable event occurs as a result of the trust ceasing to qualify as a QDOT, the amount of property subject to the QDOT tax is the fair market value of trust assets on the date of disqualification.

The deferred estate tax imposed equals the Federal estate tax that would have been imposed under section 2001 of the Code on the estate of the first decedent spouse had the property subject to the tax been included in the first decedent's taxable estate. Generally, in computing the deferred estate tax, the rate of tax is determined by reference to the actual size of the first decedent's estate, as increased by the amount involved in the taxable event.

As noted above, the death of the surviving spouse is a taxable event and the property remaining in the QDOT at that time is subject to Federal estate tax as if it were included in the estate of the decedent spouse. The property remaining in the QDOT at the death of the surviving spouse may also be included in his or her estate under section 2001 (if the surviving spouse was a United States resident at death) or section 2101 (if the surviving spouse was a nonresident alien). To avoid subjecting the property remaining in the QDOT to double tax, certain credits may apply to the estate of the surviving spouse.

Section 2056(d)(3) provides special rules for the application of the credit for tax on prior transfers provided under section 2013 of the Code regardless of the length of time between the spouses' deaths. First, if a marital deduction is allowed to the estate of the first decedent spouse (the transferor) for QDOT property passing to the surviving spouse (the transferee), the deferred estate tax imposed is treated as an estate tax paid by the estate of the transferor spouse with respect to the QDOT property. Accordingly, if the transferee spouse's estate is subject to United States estate tax under the Code, the deferred estate tax, whether imposed on distributions during the transferee's lifetime under section 2056A(b)(1)(A) or on the transferee spouse's death under section 2056A(b)(1)(B), is creditable within the section 2013 framework against the transferee spouse's estate tax.

Section 2056(d)(3) also provides a special rule affecting the application of the section 2013 credit where property included in the transferor spouse's gross estate is not deducted under section 2056(a), solely because the property does not satisfy the alien spouse requirements under section 2056(d) and 2056A (e.g., the transferee spouse elects not to transfer an outright bequest to a QDOT). Under these circumstances, on the death of the transferee spouse, if the transferee's estate is subject to United States estate tax, the allowable section 2013 credit is determined without any percentage reduction that may otherwise be required by section 2013(a).

In computing the estate tax imposed under section 2056A(b)(1)(B) on the death of the surviving spouse, a credit for state or foreign death taxes under section 2011 or 2014, respectively, is allowed only if the state or foreign death taxes are paid by the surviving spouse's estate for the QDOT (because the QDOT is included in the surviving spouse's gross estate for state or foreign tax purposes). In addition, state or foreign death taxes previously paid by the decedent/transferor's estate are also creditable within the section 2011 or 2014 framework for any federal estate taxes treated as paid by the decedent/transferor's estate.

Due Date for Payment of Tax

The deferred estate tax imposed on lifetime distributions under section 2056A(b)(1)(A) is due on April 15th of the calendar year following the end of the taxable year in which the taxable event occurs, except for taxable events which occur during the calendar year in which the surviving spouse dies. In the latter case and for tax imposed on the surviving spouse's death under section 2056A(b)(1)(B), the tax is due no later than 9 months after the date of the surviving spouse's death, unless an extension of time for payment is granted.